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IN-DEPTH REVIEW OF
INDIAN TRUST FUNDS FOR
THE BUREAU OF INDIAN AFFAIRS

TASK V
RECOMMENDATIONS

JANUARY 11, 1984



OFFICE OF GOVERNMENT SERVICES

1801 K STREET, N.W.
WASHINGTON, DC 20006
202 296-0800

January 9, 1983

Mr. John Vale
Chief, Branch of Investments
Bureau of Indian Affairs
Post Office Box 886
Albuquerque, New Mexico 87103

Dear Mr. Vale:

RE: CONTRACT NUMBER K51C14201203
TASK 5 SUMMARY OF RECOMMENDATIONS

Price Waterhouse has conducted an analysis of the Indian trust funds focusing on issues related to portfolio management and cash management. As part of our overall work, we also considered related accounting system and control issues. The recommendations that result from our analysis are summarized in the exhibit found as Attachment I.

Many of our recommendations can be implemented in a matter of weeks. Other recommendations involve major system development efforts or changes in legislation. The GANTT chart enclosed as Attachment II provides guidance for scheduling the implementation of our recommendations.

1. Portfolio Management Recommendations

We have recommended that the Bureau of Indian Affairs (BIA) develop and implement an on-going process to enable tribes and individuals to participate in the formulation of investment objectives for the Indian trust funds. In furtherance of these

objectives, we have recommended that the BIA offer tribes and individuals the option of making proportional assignments of funds among alternative portfolios designed to meet specific objectives.

As is often the case when implementing new procedures and assigning new responsibilities to field personnel, it is easy to underestimate the time and effort required for:

- o Preparing procedural documentation
- o Training field staff
- o Educating trust fund beneficiaries to the objective-setting process

Consequently, we have suggested that, initially, only the following two portfolio options be provided:

- o A short-term highly liquid portfolio
- o A medium term wealth maximization portfolio

We estimate that it will take six months to structure the portfolios and develop the procedures. We anticipate that it will take an additional fourteen months to implement these procedures.

In order to maintain the credibility of the investment process and to provide for policy level decisions regarding portfolio management, we have recommended that a formal oversight committee with public and private sector representation be established. The oversight committee will review the investment strategy for managing the portfolios and undertake periodic

review of trust fund performance. Thus, the Committee should be empaneled as soon as practicable.

Among the responsibilities of the oversight committee will be the selection of outside investment advisory services. In our view, an investment advisory service will assure that the BIA will have access to experienced portfolio managers, who may not be available in the future from sources within the government.

The investment advisory service will also assure continuity in the day-to-day management of the Indian trust fund portfolios. The advisory service will provide assistance in selecting securities to meet the policy objectives established for trust fund portfolios by the oversight committee.

As the portfolio management recommendations are implemented, we anticipate that the need will increase for enhanced reporting to the beneficiaries of the Indian trust funds and to senior management within BIA. For this reason, we have recommended that BIA adopt report formats and report frequencies comparable to those in use at financial institutions that have in excess of \$1 billion under management.

We have further concluded that implementation of all of our recommendations in the portfolio management area will require more formal procedures to structure the interaction of trust fund beneficiaries with the Branch of Investments. This implies that a more active role will be created for area and agency investment coordinators. Our Task III and IV reports have a further description of such a role.

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2. Cash Management, Accounting System and Control Related Recommendations

Within these areas, we have developed a broad program for the enhancement of Bureau activities. As a first overall priority, we recommend that immediate attention be directed to improving controls, procedures and organizational assignments, as related to current systems and activities. Many of the control improvements described in our Task IV report can be implemented without costly changes to existing computer systems. In addition, subsequent implementation of new systems should be made in an effectively controlled environment.

As the next priority, we recommend that improvement modifications be made to the systems and procedures related to both Cash Management and Trust Fund Accounting. As a general principle, we have minimized the instances where the Bureau would have to design and implement new complex computer-based systems. As such, we have recommended the purchase of processing services from external providers (banks or data processing service organizations), to provide the most timely and cost effective system solutions. These services are currently used in the private sector and would be available and applicable to BIA. We have also recommended incremental approaches to implementing change, whenever possible. Rather than moving rapidly to relatively complex solutions, BIA can improve its activities in steps, over a period of time, making implementation within the organization much easier.

In terms of more detailed implementation actions, BIA should first designate specific individuals, with supporting staff as necessary, within the Branch of Investments to be responsible for

cash management, and within the Office of Finance and Accounting (or reporting directly to the Assistant Secretary as described in the Task IV report) to be responsible for trust fund accounting. These individuals would also be responsible for the improvement projects to be conducted over the next several years and for operation of the relevant new systems as they are implemented.

As an additional first step, we recommend that the BIA undertake an effort to assess the quality of existing financial data. An audit of the balance sheets of each of the trust funds should be conducted. Upon completion of such an effort, the Bureau would be better equipped to plan the conversion related to the implementation of any new systems.

Our Task IV report describes an Accounting and Control System Action Plan. This Plan includes recommendations in the areas of policy/procedures and automated systems. Within the areas of policy/procedures our major recommendations are as follows. These recommendations should be implemented within approximately eight months.

- o Define more clearly the responsibilities of trust fund financial management officials. Among the initial actions to be defined should be more frequent and timely reconciliations of key systems, production of periodic financial statements for each of the trust funds, and appropriate reviews of all activities by independent parties.
- o Prepare an up-to-date Policy and Procedure manual for both the Central Office and Agency Offices.
- o Segregate the tasks of investment management and security custody.
- o Establish an ongoing financial audit function. This should include both the establishment of an internal

audit group and arrangements for timely annual audits by an outside party (either governmental or private sector).

With respect to automated systems, our longer-term recommendations are as follows:

- o Implement a trust accounting system. Such a system would account for the assets and liabilities of the Trust Funds separately from the appropriation related activities of the BIA and could be run through an external service organization which would provide terminal access in Albuquerque. Ultimately, a fully implemented trust accounting system could replace several existing BIA systems used for trust accounting and investment management.
- o Implement a Bureau-wide system to account, at the individual account level, for Individual Indian Monies. Such a system should provide both local and central access to individual Indian accounts and allow central application of receipts which must be applied to a large number of individual accounts.
- o Implement an improved system for tracking expected income. Most leases or contracts establish due dates and procedures. Effective management of trust assets dictates the need for a system to insure the timely receipt of payments due.

Our Task IV report also includes a Cash Management Action Plan. This plan describes incremental improvements to current activities based on the following sequence of changes:

- o Implement a deposit reporting service to provide the Branch of Investments with reliable daily information of all local deposit activities. This would involve the procurement of services from a commercial vendor and would not involve the installation of software on BIA's computers. Our preliminary estimate is that such a system could be in use within four months.

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- o ~~Modify cash deposit procedures by the~~ (1) ~~establishment~~ of local depositories at those agencies currently lacking this capability; (2) establishment of BIA trust fund concentration accounts in a major commercial bank (outside of the U.S. Treasury); and (3) utilization of a balance reporting service from the commercial bank selected for the concentration accounts. These changes could be phased in, starting with a small group of agencies and gradually extending to all agencies.
- o Consider a shift of BIA disbursement activities away from the U.S. Treasury to the concentration bank noted above. With this arrangement, checks would be drawn on the concentration bank and the trust funds would obtain the benefit of the disbursement float.

* * * * *

This Task V report completes our work pursuant to the subject contract. We trust that our recommendations will assist the BIA in enhancing its activities relative to the Indian trust funds. We have been pleased to participate in this significant engagement.

Very truly yours,

The logo for Price Waterhouse, featuring the word "Price" above "Waterhouse" with a stylized "P" and "W" that overlap.

DRAFT

RECOMMENDATION SUMMARY

Portfolio Management

Branch of Investments

- o Establish alternative portfolios that meet distinct objectives for Indian trust funds.
- o Allow tribes and individuals to make proportional assignments of funds among portfolios.
- o Extend portfolio alternatives to meet tribal and individual requirements, where sufficient subscriptions can be solicited.
- o Manage portfolios initially, using a passive diversification strategy.
- o Adopt immunization and active portfolio strategies as the need arises and management resources become available.
- o Pool the tribal trust fund for investment purposes.
- o Obtain external investment management services under an advisory arrangement.
- o Establish Investment Policy Oversight Committee with private sector representation.
- o Separate portfolio management function from transaction execution function.
- o Establish formal research and portfolio monitoring function.
- o Seek authorization to enter into a discretionary account arrangement with an investment advisory firm.
- o Enhance trust fund performance reporting.
- o Investigate methods to offset implicit transaction costs associated with portfolio management with explicit user fees.

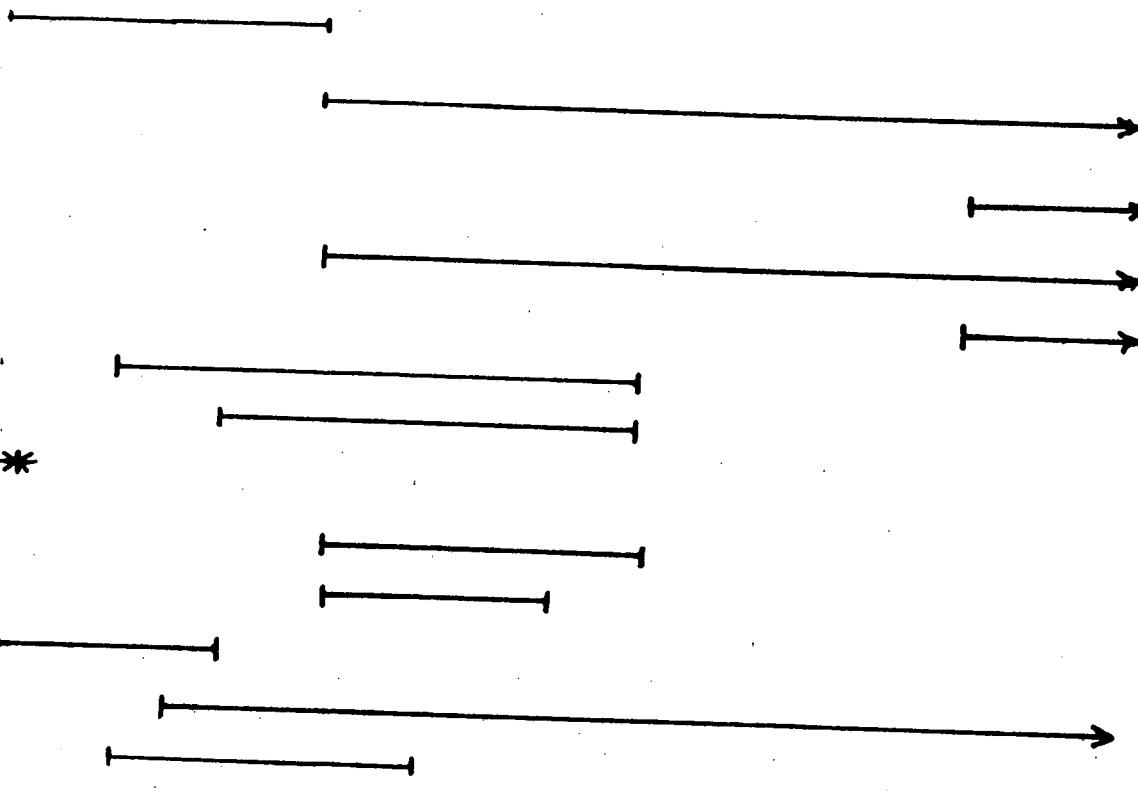
Cash Management, Accounting,
System and Controls

- o Establish cash management function (an officer)
- o Improve cash management in three stages.
 - Employ a deposit reporting service
 - Modify cash deposit procedures
 - Establish local depository arrangements
 - Establish accounts in a commercial bank
 - Employ a balance reporting service
 - Shift disbursement accounts from the Treasury to the concentration bank
- o Segregate security custody and investment function
- o Standardize contracts requiring EFT and monitoring of late payments.

Branch of Investments

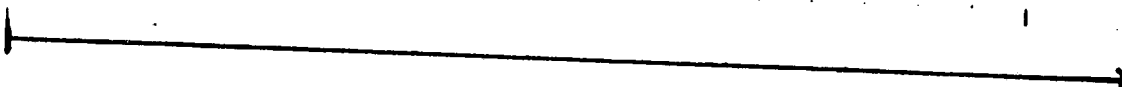
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- o Establish alternative portfolios that meet distinct objectives for Indian trust funds.
- o Allow tribes and individuals to make proportional assignments of funds among portfolios.
- o Extend portfolio alternatives to meet tribal and individual requirements, providing that a minimum level of subscriptions can be solicited.
- o Manage portfolios initially, using a passive diversification strategy.
- o Adopt immunization and active portfolio strategies as the need arises and management resources become available.
- o Pool the tribal trust fund for investment purposes.
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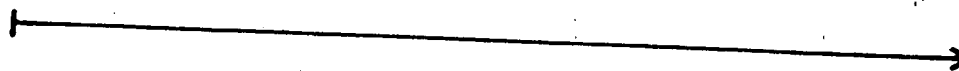
Area Office

- o Provide assistance through investment coordinators to tribes in setting investment objectives and selecting among portfolio alternatives.



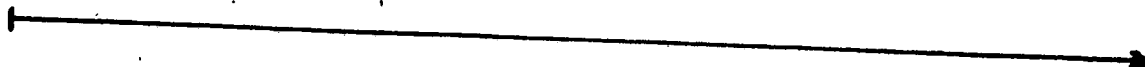
Agency Office

- o Provide assistance to individuals in selecting among alternative portfolios.



Finance and Accounting

- o Produce data to support daily deployment of assets report and cash position report.



Branch of Investments

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- o Establish cash management function (an officer) *
- o Improve cash management in three stages.

- Employ a deposit reporting service

- Modify cash deposit procedures

- Establish local depositary arrangements

- Establish accounts in a commercial bank

- Employ a balance reporting service

- Shift disbursement accounts from the Treasury to the concentration bank

- o Segregate security custody and investment function

- o Standardize contracts requiring EFT and monitoring of late payments.

Area Office

- o Increase wire transfer of payments to trust funds

Agency Office

- o Deposit over-the-counter receipts in local bank for wire transfer to the Treasury or concentration bank.

- o Impose appropriate controls over cash handling.

Office of Administration

- o Establish the position of trust fund accounting officer *

- o Establish internal and external audit functions

- o Commission of external (GAO or private sector) audit of trust fund assets

Finance and Accounting

- o Improve accounting systems using purchased services.

- Implement trust accounting system

- Implement IIM system

- Implement income tracking system

- o Update accounting policies

Schedule begins when tasks with *'s are complete!